

TESTIMONY OF THE  
THE AMERICAN SOCIETY OF TRAVEL AGENTS, INC.  
Before the  
UNITED STATES SENATE  
COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION

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## **Testimony of the American Society of Travel Agents**

The American Society of Travel Agents (“ASTA”) is pleased to provide the Committee with the perspective of its travel agency members on the nature and extent of competition in the airline industry as it relates to the distribution system and on the issues raised by S. 383, the Airline Passenger Fairness Act (Sens. Wyden and McCain) and S. 477, the Airline Competition Act of 1999 (Sen. Schumer). These views are also presented on behalf of the Coalition for Travel Industry Parity (CTIP), with which ASTA is allied in the pursuit of numerous legislative and industry objectives to assure that travel agencies and the traveling public have unimpeded access to each other.

ASTA was established in 1931 and is today the leading professional travel trade organization in the world. Its travel agency members account for more than half of the 29,000 staffed, agency locations serving the public throughout the United States. ASTA's corporate purposes specifically include promoting and representing the views and interests of travel agents to all levels of government and industry, promoting professional and ethical conduct in the travel agency industry worldwide, and promoting consumer protection for the traveling public. ASTA has provided testimony to numerous legislative committees and fact finding bodies and has appeared in various legal proceedings; it is widely recognized as responsibly representing the interests of its members and the travel agency industry.<sup>1</sup>

CTIP is a coalition of 23 travel agency co-operative, consortia, and franchise organizations with about 17,000 travel agency members.

Together ASTA and CTIP represent most of the travel agencies in the United States.

### **The Consumer Fairness Issues**

In the summer of 1998, ASTA introduced its own Air Travelers' Bill of Rights, a nine-point code of principles. Recognizing that the airlines use the public air space and public facilities to profit from the transport of millions of people who have no

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<sup>1</sup> See e.g. Investigation into the Competitive Marketing of Air Transportation, C.A.B. Docket 36595, aff'd; Republic Airlines, Inc. v. C.A.B., 756 F.2d 1304 (8th Cir. 1985); In re Domestic Air Transportation Antitrust Litigation, 148 F.R.D. 297, 61 USLW 2610, 1993-1 Trade Cas.(CCH) ¶70,165 (N.D.Ga., 1993); U.S. v. Airline Tariff Publishing Co., 1993-1 Trade Cas. (CCH) ¶70,191 (D.D.C., 1993); Spiro v. Delmar Travel Bureau, Inc., 591 N.Y.S.2d 237 (A.D. 3 Dept. 1992); and Crowder v. Kitagawa, 81 F.3d 1480 (9th Cir. 1996).

alternative but to use their services, the bill of rights says in its preamble that, “ circumstances compel the airlines to accept a special public trust and responsibility to comply with minimum standards of courtesy, comfort, convenience, and service. All passengers should be treated with respect and awareness that they are the owners of the public air space.”

Under the ASTA “Air Traveler’s Bill of Rights,” a consumer has the right to:

Truth in advertised prices, schedules and seat availability

Equal access to unbiased, comparative travel information and all fare and service options

A comfortable seat, reasonable space for carry-on luggage, healthful meals, and clean sanitary facilities, regardless of class of service

Timely and courteous assistance in making connections

Use all, part or none of the segments on any ticket purchased

Timely, complete and truthful information and courteous assistance regarding delays, cancellations, and equipment changes

Timely and courteous assistance for the disabled and unaccompanied children

Appropriate in-flight medical emergency assistance

Access to the courts and state consumer laws to resolve disputes with airlines.

We called upon the airlines to adopt the code as their own. Their response, through the Air Transport Association, was that the Air Travelers’ Bill of Rights was just sour grapes by travel agents who were miffed over airline reductions of commissions. Rejecting the mounting evidence of the rising tide of public dissatisfaction with the delivery of air travel services, the airlines maintained that there was no real problem and thus that no focused solution was necessary or appropriate.

This winter the pot boiled over when Northwest Airlines held passengers inside aircraft unable to take off due to weather at Detroit for seven and more hours. More recently, the “sick out” by American Airlines’ pilots further enraged the public, many of whom saw themselves as pawns in a chess game played by two largely indifferent

combatants. These incidents may be unusual, but they served as graphic illustrations for many that the airline industry, while delivering extraordinarily safe transportation, is not sufficiently concerned with the issues of comfort, courtesy and respect for the people who ultimately pay the bills.

ASTA believes that the time has come to compel the airlines to recognize the primacy of the air travel customer and to establish national standards of performance in key areas such as those identified in the ASTA Air Traveler's Bill of Rights. The forces of competition are not disciplining the airlines' behavior in the way that was anticipated when the Airline Deregulation Act was passed in 1978. Absent intervention by the Congress, there is no reason to expect the airlines to respond differently than they have in the past.

For those reasons, ASTA and CTIP support the prompt enactment of S. 383, the Airline Passenger Fairness Act, as well as S. 477, the Airline Competition Act of 1999, insofar as those bills address the issues of airline treatment of passengers.

### **Consumer Access to Information Issues**

The bills before the Committee, and other bills pending in the House of Representatives, contain numerous provisions dealing with airline competition, in areas such as airline predation against new entrant competitors, slot allocations, perimeter rules at restricted airports, hub competition and other similar issues. These are very important issues and deserve thorough attention by the Congress. If the engine of competition is not restored to full vigor, the consumer benefits foreseen to arise from airline deregulation will be lost. Once lost, they will be extremely hard to regain. We leave the details of that debate to others more directly involved with those issues.

We deeply believe, however, that even if the Congress and other relevant government bodies act aggressively on those direct airline competition issues, but do not attend to the related issues arising from the airlines' attempt to subvert the retail distribution system, the battle over predation and other details may be won while the larger and more important war to preserve competition will be lost.

We refer to the pattern of policies and practices adopted by most of the large airlines that are designed, and are having the effect, of making it more difficult for consumers to continue accessing the services of the only source of neutral, comparative price and service information, as well as expertise and personal advice, that exists – the travel agency distribution system. We have set out below in detail the nature of the policies and practices that the airlines are using to hamstring the travel agent and the traveling public. The goal is to force the public to deal directly with biased sources of information provided by the airlines themselves.

If successful in this effort, the airlines will enjoy an enormous economic windfall at the

expense of the public. Deprived of easy access to neutral, comparative information, the traveling public will, inevitably, make mistakes in air travel purchases, paying higher than necessary fares when there were cheaper alternatives and getting less optimum service for the travel dollars they spend. The ability of consumers to make optimal choices depends upon their having access to good information about the full array of choices available to them. That is the service that travel agencies have been providing so effectively since airline deregulation and which has led about 80 percent of the air traveling public to prefer agents as their source of information and travel documents. The Congress must act to prevent the airlines from monopolizing the distribution function.

For those reasons, ASTA and CTIP urge immediate enactment of the portions of S. 383 and S. 477 that compel the cessation of these practices or direct the Department of Transportation to investigate and report to Congress on them.

We have set out below an updated version of the testimony ASTA recently provided to the Committee for a Study of Competition in the U.S. Airline Industry, Transportation Research Board of the National Research Council, National Academy of Sciences, elaborating on the ideas summarized above.

### **Background**

As Alfred Kahn, the acknowledged “father” of airline deregulation, has observed, deregulation can continue “only in the presence of effective competition as the protector of consumers.” Both economic theory and practice within the air transportation industry support the conclusion that the availability of comparative information about air transportation services is beneficial to vigorous competition among the airlines and necessary to the maintenance of affordable fares and responsive services throughout the country. Since 1978, the stated policy of the United States, as manifested in the Federal Aviation Act of 1958, amended by the Airline Deregulation Act of 1978, has been to promote aggressively conditions of competition between and among the airlines.

Travel agents provide two crucial services essential to assuring the competitive environment necessary for the public to benefit from, rather than be victimized by, airline deregulation.

First, they facilitate entry, exit and price and service competition among existing and new entrant airlines. Agents provided every carrier, in every market, an instant professional distribution system ready and able to inform the public of service and price options and to sell all of the inventory available at any moment, with no additional investment required by the airlines.

Second, travel agents promote the use of air transportation services by the public by

serving as the only one-stop, neutral source of comprehensive information and counseling about an incredibly complex, constantly changing array of fares and services.

During the early years of deregulation these functions of the professional full-service travel agency served the needs of the airlines very well. Once the airlines' ability to fix commissions by agreement was ended by the Civil Aeronautics Board, competitive forces led to the expected and inevitable rise in agency compensation to the level of 10 percent of the fare sold as a "base commission" for all transactions. Travel agencies made rapid competitive maneuvering possible in an environment where the race went to the swiftest. As the airlines adapted to the new competitive marketplace, they earned considerable profits during the 1980's. Deregulation thus produced benefits for the major airlines as well as the traveling public.

Travel agencies also benefitted. The public liked what travel agencies did for them, and they flocked to agencies for help with the morass of fares and schedule changes that deregulation produced as the necessary corollary to a free market. The market share of travel agencies for air transportation rose from a pre-deregulation level in the low 40 percent range to about 80 percent for domestic sales and over 90 percent for international business. Travel agencies account for more than \$120 billion in travel sales annually, some seventy percent of which is air transportation.

Travel agencies continued to do well even when the fortunes of the airlines turned down in the early 1990's.<sup>2</sup> The airlines lost billions a year while agency sales continued to rise (save only for the Gulf War year of 1991).

More recently, with the consolidation of the industry into a handful of giant carriers, and with various other types of alliances being almost routinely approved by the Government, these large airlines began to recognize new fundamentals of the competitive market that had evolved. First, they saw that travel agents were a potential obstacle to their objectives; agents made sure that consumers fully understood all of the fare and service options open to him. Second, the airlines came to understand that consolidation of the airline industry, combined with the success of passenger loyalty programs, had yielded genuine market power for the airlines over the travel agencies. Third, for the first time, an apparent alternative to distribution through travel agencies had emerged: the Internet, by which the airlines believed they could control directly the information provided to the public without meddlesome interference by travel agents telling a somewhat different, and unbiased, story.

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<sup>2</sup>The agencies' share of airline sales rose from 55 percent in 1977 to 81 percent in 1995. P. Ruden, Competition in the Distribution of Travel Services 5 (ASTA 1997).

## **The Airlines' Strategy**

Armed with motive and opportunity, the airlines have now embarked on a campaign to reshape the market in their own image. Their deliberate course of conduct, described below, has substantially reduced competition in the market for travel services and injured consumer welfare. If successfully consummated, this strategy will make it much harder for the public to learn about all of the fare and service options available to them and thus increase the likelihood that they will, on the whole, spend more for air travel than they otherwise would. By restricting access to unbiased and comprehensive information from independent sources, the airlines expect, rightfully, that they will be able to increase the average price consumers pay for air travel.

Travel agents quote schedules and fares, and provide ticketing services, to consumers on major U.S. airlines, small U.S. airlines, large and small international airlines, and start-up airlines. Travel agents are the only efficient, independent and comprehensive neutral sources of information for airline travel options. Travel agency sales of air travel alone exceed \$80 billion annually.

If the airlines can divert any meaningful amount of this business to themselves, the potential gain to them is enormous, not merely in commissions avoided, but in the higher overall prices that consumers will pay for air travel. Deprived of easy access to independent sources of comparative price and service information, consumers inevitably will end up paying more, on average, even if the airlines never raised another fare.

Nor are the changes the airlines are aiming at the distribution system in furtherance of their strategy occurring under conditions of a level playing field in which consumer preferences ultimately control the outcome. Instead, the airlines are using market power, collective activities and other devices to undermine the distribution system to achieve their goal of reducing the public's access to independent comparative price and service information.

These actions include: reducing commissions to below compensatory levels, discriminating against agency transactions originating on the Internet with non-compensatory commissions, discriminating against agencies with respect to fare policies in ways that interfere with agency-client relationships, and using the Airlines Reporting Corporation and other collective activities to compete unfairly with travel agents.<sup>3</sup>

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<sup>3</sup> One airline, United, in 1998, has gone so far as to purchase national advertising that falsely disparages travel agencies' services. Their ad states: "If you want it done right, come to us!" "Us," refers to a computer program at [www.ual.com](http://www.ual.com).

### *Non-compensatory Commission Policies*

The first action in the airlines' anti-consumer campaign began in 1995, when the major airlines, save only Southwest Airlines, capped travel agency commissions at \$50 per round-trip ticket. This was followed in September, 1997, with across-the-board reductions in the domestic base commission rate from 10 percent to 8 percent. In dollar terms, the total compensation reduction to agents is more than 30%.<sup>4</sup>

At this time, consumers have overwhelmingly elected to continue to do business with travel agents, but millions of consumers now pay transactions fees to agents, fees which agents have been forced to adopt to off-set airline commission cuts. Consumers who are unwilling or unable to pay travel agent transaction fees must contact airlines directly and often pay higher fares as a result. As airlines continue to reduce agency commissions, many consumers may be willing to pay higher fees for the right to do business with agents, but millions of other consumers will be forced to deal directly with major airlines.

This puts the consumer right where the airlines want him, bereft of a neutral source of information to deal with a bewildering array of complex air fares and services. As travel agents are forced out of the industry and airlines secure more direct consumer business, consumer alternatives will continue to decrease resulting in significantly higher consumer travel costs. This "revenue squeeze" has made entire segments of airline ticketing activity non-remunerative for agents, a major factor in the exit of 12 percent of independent U.S. travel agencies from the industry during 1995-98, as well as in a shifting of resources by the remaining agencies to non-air sales. This is the first decrease in the number of travel agencies since World War II, and more closings are expected as agency operating reserves are exhausted.

Small domestic airlines, many international airlines, and start-up airlines who depend upon the travel agency distribution system will be adversely impacted if not eliminated. There is no alternate distribution system available to these types of airlines.

Major airlines have generally misrepresented the reason for agency commission cuts, citing a need to reduce expenses and pass savings on to consumers. In fact, airline ticket prices have steadily increased, and airlines are posting record profits quarter-after-quarter. Not one penny of the alleged cost savings can be discerned to have been passed on to consumers through better service or lower ticket prices. There have been no consumer benefits... and consumers are paying the highest airfares in history.

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<sup>4</sup> The commission rate for July, 1998 domestic air transactions was 6.70 percent according to official Airlines Reporting Corporation reports. In January, 1995, before the commission caps, the rate was 10.01 percent.

### *Agency Transactions Originating On The Internet*

Major airlines have also all but eliminated Internet competition by travel agents, by adopting discriminatory and non-compensatory commission policies for bookings originated on-line. As with conventional distribution, Internet consumers have very limited ability to view consolidated electronic schedule and fare information, much less interpret the rules, restrictions and penalties attached to such lower fares as might be found.

Commissions paid to on-line travel agencies and other independent on-line ticketing services are at a rate of 5 percent with a \$10 maximum, which is well below these firms' costs. The airlines have thereby succeeded in arresting in its incipiency an effective counter-measure available to agencies to offset reductions in commissions on traditional sales: unfettered access to consumers through high-volume, low-cost electronic marketing systems.

Most recently, in implementation of the airlines' non-compensatory Internet transaction policies, their jointly owned alter ego, Airlines Reporting Corporation ("ARC") has begun issuing special numbers called Electronic Reservations System Provider numbers ("ERSP" numbers). At least one airline has informed travel agents that they must attach these special numbers to every transaction that originates on the Internet. The only apparent purpose for this requirement is to help the airline enforce its discriminatory commission policy with regard to Internet transactions.

In this scenario, the airlines, through ARC, are collectively facilitating the enforcement of commission policies designed to keep travel agents from becoming meaningful participants in the electronic marketplace.

One reputable commentator on travel consumer matters summed up the current state of affairs as follows:

"The reason the online dream is dead, is that the airlines want it dead. If online travel agencies were to succeed at finding customers the tickets they want at the lowest prices, they would quickly dominate the retail travel business- and squeeze much of the profits out of the passenger airline industry. The airlines are not standing by and letting this happen."

Craig Stolz, "The E-Travel Revolution Is Over," Washington Post, November 15, 1998, at E-5.

### *New Entrant Obstacles*

For at least the second time since airlines were deregulated, the so-called “new entrant” airline group, which typically operates on a no-frills, low-cost, and thus low fare, economic model, is finding it difficult, often fatally so, to compete with major established airlines. Major airlines monopolize airport facilities, earn huge returns from the computer reservations systems they control and own (and through which almost all airline reservations are made), target small carriers using massive giveaways (such as frequent flyer program points), and employ temporary fare-cutting tactics to deter or block new market entry.

A competitive market for travel services, i.e., one in which consumers anywhere in the U.S. can readily turn to independent agents to reduce search costs and avoid buying errors, makes it possible for new carriers to enter the market and for small carriers to expand without bearing the full costs of second-stage entry (developing their own distribution network). Thus, carrier practices that restrain the ability of agents to compete also tend to raise entry barriers in first-stage markets in which carriers compete among themselves. Federal agencies such as DoJ and DoT have long been concerned about market conditions that impede entry and expansion of small, low-price carriers, and there is good reason to believe that erosion of travel agency competitiveness will translate directly into less competition in the market for air transportation.

Moreover, market imperfections, including consumers’ notorious lack of information about carriers’ complex, ever-changing and often poorly visible price and service offerings, enable carriers with market power over particular routes and facilities to discriminate against captive consumers. By restricting travel agencies’ output, individual airlines can and do exercise and maintain market power in discrete geographic markets for air transportation, especially city-pairs involving a “hub” where the carrier is the dominant or monopoly provider.

If the major airlines are successful in destroying most or all of the smaller, new entrant airlines, competition in airline pricing and schedules will diminish even further.

### *Discriminatory Ticketing Policies*

Major airlines refuse to permit agents to offer certain benefits and concessions to consumers, such as the refund of so-called “non-refundable” tickets, while reserving to themselves the right to make such refunds. Transgressions are punished severely with airlines levying cash penalties against agents to which agents are summarily required to acquiesce or face the greater penalty of losing their ability to issue tickets altogether. Yet the airlines themselves often issue such refunds. The airlines then typically force the agent to repay the commission earned on the original sale.

Similar discrimination in competitive practices occurs with respect to price-saving opportunities such as the sale of “back-to-back” and “hidden city” tickets, as well as

highly publicized special fares, that require consumers to purchase directly from airlines. These discriminations have the consequence of interfering with the relationship between the travel agency and its clients, by, among other things, impairing the agency's credibility in the eyes of the customer.

"Back-to-back" tickets, are a pair of tickets issued to permit the traveler to avoid the Saturday night layover normally required to get a discounted ticket. Airlines prohibit agents from issuing these tickets, and normally demand the agent pay the full coach fare as the penalty for so doing.

"Hidden city" tickets, in which the passenger buys a ticket A-B-C, which is cheaper than a non-stop A-B ticket, then gets off the plane at B, are also forbidden and punished severely. In addition, major airlines, while acknowledging passenger contracts for passage legally exist only between passengers and airlines, nonetheless reserve the right to penalize travel agents financially when consumers buy inexpensive round-trip tickets, travel one-way, and throw away the return portion of the ticket. Such policies confuse and anger the public, while undermining the relationship between the travel agent and his client, who expects the agent to find and ticket the lowest fare available.

Airlines have also adopted an identical condition upon redemption of frequent flyer awards that arbitrarily forces consumers to by-pass agencies. These awards are mostly earned at employer expense but are commonly used by individual travelers for leisure trips, many of which would have been arranged through travel agencies. The airlines divert substantial revenue from agencies by requiring awards to be redeemed directly from airlines.

As recently as January 11, 1999, Delta Air Lines announced initiation of a \$1 surcharge for each published fare component on all U.S. domestic fares. Under this scheme most round-trip tickets, which are constructed using two fare components, would include a \$2 surcharge. Additional surcharges would apply on tickets constructed using multiple fare components. This surcharge, however, would not be applied to tickets issued via Delta's SkyLinks Internet web site.

Thus, Delta's scheme penalized all of its customers who wished to avail themselves of the opportunity to receive comparative cost data by consulting a travel agent. The avoidance of the \$1 surcharge penalty by using the Delta web site is "fools gold" placed in consumers' paths to lure them into remaining in the dark about fare alternatives that could potentially save them hundreds of dollars.

Delta cited increased computer reservation system ("CRS") booking fees as its justification for this punitive charge for using a travel agent --- a rationale reminiscent of the late comedian, Flip Wilson's signature line, "the Devil made me to it." Since the airlines by and large own the CRS systems, they are both responsible for, and benefit

directly from, the increased CRS booking fees of which Delta complained.

In this case, at least, the public outcry was so great that the other airlines declined to match the Delta surcharge. It was dropped after a few weeks. Delta nonetheless stated that any passenger seeking to get credit for having paid the \$1 surcharge would have to pay a \$75 change fee that Delta imposes on discount tickets.

### *Airlines Use of Joint Assets*

The airlines also use discriminatory collective or joint operation of assets to offer concessions, benefits and services to the public while denying comparable access to such concessions, benefits and services through travel agents and other independent air transportation distributors, including, but not limited to, joint sales activities, denial of competitive tools, and denial of distribution efficiencies. The airlines operate several collective businesses that are used to disadvantage travel agents and to limit public access to comparative price and service information.

These include ARC, which controls both who can become a travel agent and the settlement of funds between travel agents and the airlines. ARC is also involved in the formatting of standard agents' ticket stock. When the airlines cut commissions in 1997, the travel agency community sought the inclusion on the ticket document of a space where the agent could insert its own service fee and process the charge through ARC along with fares, taxes, and other charges on the ticket. The airlines have made it clear that this important competitive efficiency mechanism will not be provided to travel agents.

More recently ARC has begun providing "accreditation" of corporate customers, purporting to make them "agents" of the airlines that sell to them, so that the corporations can have standard travel agents' ticket stock and settle accounts with the airlines through the same system used for travel agents. In purpose and effect, this program is collective action that facilitates the carriers' strategy. Among other things, it enables them jointly to target, select, large volume corporate accounts that constitute a

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<sup>5</sup> As Justice Brennan, observed, concurring in White Motor Co. v. U.S., 372 U.S. 253 (1963):

Instead, [defendant] seeks the best of both worlds to retain a distribution system for the general run of its customers, while skimming off the cream of the trade for its own direct sales. That, it seems to me, the antitrust laws would not permit...

large and lucrative source of agency profitability and skim the “cream”<sup>5</sup> for themselves. This program also clearly exceeds the scope of joint activity permitted under the Justice Department’s December 26, 1984 Business Review Letter announcing it would not challenge ARC’s proposal to administer travel agency accreditation under defined terms and conditions.

Another example, until quite recently, was the operation of SATO, Inc., the functional equivalent of a mega-sized travel agency that the airlines collectively owned and used to compete with travel agencies for government and corporate business.<sup>6</sup> The airlines claimed that SATO was more cost-effective than travel agencies and was operated on a non-profit, strict cost-pass-through basis, but there was evidence that the actual cost of SATO on a percentage-of-ticket-price basis was several points higher than the average actual cost of travel agency commissions. And when the airlines capped travel agent commissions, no reduction was placed on SATO’s working “commission,” thus increasing the advantages it had over regular travel agencies.

In fact, exempt from the same commission caps and ticketing restrictions that the carriers have imposed upon travel agencies, SATO enjoyed an effective commission rate of approximately eleven (11) percent, or about twice as much as agencies’ average gross commissions on air sales. Moreover, SATO no longer limited its activities to the government travel market, which was the sole focus of its business when the Justice Department issued its May 2, 1986 Business Review Letter allowing this joint airline venture to go unchallenged. SATO has now been sold, but its historical collective use as an unfair competitive weapon against travel agencies remains a fact.

#### *Agents’ Transaction Data*

One of the most egregious of the airline practices in question, is the process whereby the airlines share competitively significant sales transaction data in violation of the

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<sup>6</sup> Since this paper was first written, the airlines have announced that SATO, Inc. has been sold to private investors who will operate it as a travel agency. We do not know at this time with certainty whether a special relationship between SATO and the airlines will survive this sale.

confidentiality interests of the travel agents and other independent air travel distributors who generated the transactions.

Confidential business information generated by travel agencies is routinely captured and shared by the airlines in a manner that would be blatantly unlawful absent regulations issued by the Department of Transportation. Those regulations require each computer reservations system (most of which are controlled by airlines) to make available to all participating U.S. airlines all marketing, booking and sales data that it generates from its systems.

In addition, ARC sells to airlines travel agency "total sales" figures, information that would normally be confidential unless a business consented to its disclosure. Because airlines are major competitors of travel agencies, there are serious questions as to whether they should have access to proprietary data of this kind.

If competitors in any other industry were to sit around a table and exchange this type of information in the ordinary course of business, we believe that the Department of Justice would lower the antitrust boom on them. Yet the airlines are free to share competitive information about their operations with their competitors without apparent concern. And the information is then used to disadvantage the travel agency, the only independent source the public has for neutral, comparative information.

## **Discussion**

Consumers must have access to travel agents and other independent distributors who provide unbiased consolidated schedule and fare information if we are to preserve competition in the airline industry and maintain a system that provides the public with a broad range of options, including access to small airlines and start-up carriers.

Since deregulation, the public has had the choice of buying directly from suppliers such as airlines at no additional cost and overwhelmingly has chosen to deal with travel agencies. Consumers prefer dealing with travel agencies rather than airlines when purchasing air transportation because agencies deliver far more value, convenience and services.

Among the most basic functions performed by travel agencies is to collect and distribute comparative information and advice about the price and quality of travel suppliers' offerings—a function that no single airline can or wants to perform. In addition, consumers' transaction costs are often lower than direct-dealing with airlines, especially because many travel arrangements are joint purchases of the products of several travel suppliers (for example, air transportation and hotel/rental car). In short, one-stop shopping for accurate and unbiased travel services at a travel agency is the essence of the benefit to the public, as against airlines' direct selling methods.

Yet, the major airlines have twice reduced commissions to travel agents, forcing many to charge additional fees directly to air travelers. At the same time, these airlines have instituted non-compensatory and discriminatory commission policies for travel agent bookings initiated over the Internet.

It can no longer be assumed, that, even with new technologies, travel agencies will be able to function in the future as independent sources of the services that consumers value. Slowly but surely, in a myriad of ways including those we have identified above, and in cumulative effect, the major U.S. airlines are destroying the competitiveness of travel agencies and, thereby, extracting ever-higher effective prices for air travel from consumers.

In lock-step, each of the major carriers (American, Delta, Northwest/Continental and United) that comprise the U.S. airline oligopoly, has imposed virtually identical restraints upon independent travel agencies, for the purpose and having the effect of, depriving consumers of the benefits of free and open competition. Specifically, the restraints we have identified, are designed to impede and prevent travel agencies from offering a full range of consumer services and thereby cause travel purchasers to by-pass agencies in favor of direct-dealing with carriers.

The ultimate objective and actual effect of this strategy is to warp the normal discipline of the market place and enable each airline to achieve more than competitive profits by exploiting consumers' inability to search out and obtain the lowest possible ticket prices. In other words, these restraints make possible an adverse impact upon consumer welfare much like that one would expect from traditional cartel behavior.

No airline can be expected to provide the public with unbiased comparative price and service information about its competitors. Consumers may be able to get some of this information from airline-controlled Internet sites, but the fundamental airline strategy of disabling the travel agency distribution system will leave millions of consumers without effective access to neutral comparative information.

Indeed, the unsurpassed efficiency and effectiveness of travel agents at the daunting task of gathering, sorting, analyzing, and providing advice with respect to the bewildering array of alternatives that make up today's air transportation options has been repeatedly demonstrated.

On its 9:00 p.m. e.s.t, January 19, 1998 broadcast of its "20/20" television news magazine program, ABC-TV presented a segment in which a travel agent was shown to consistently quote a lower fare for given city pairs, under identical conditions, than a reporter could obtain by calling the airlines. Co-host Hugh Downs summed up: "But a good rule of thumb is that a good travel agent can do better than you can."

The "20/20" segment confirmed the findings of an earlier, November, 1997, independent study from the U.S. Public Interest Research Group ("PIRG"), which, in

turn, confirmed PIRG's previous 1996 study. In the PIRG study, on October 9 and 10, 1997, PIRG staff, students and volunteers telephoned 8 to 10 travel agents and as many as 5 airlines in each of 28 cities, to obtain quotes for the "lowest" airfares for specific round trips originating in that city. Full fares, 1-week advance and 3-week advance fares were obtained for the departure/return dates of: (1) Thursday, October 16/19, 1997 and (2) Thursday, November 6/9, 1997. All quotes included a Saturday night stay. Departures were requested around 5 p.m. and returns around 6 p.m. on both dates.

The PIRG callers expressed flexibility to depart from any airport serving a multiple airport city, and the willingness to make one stopover. Tickets were not booked, since booking tickets would have change the pricing structure of that particular flight. The study found that the lowest fares were obtained more often from travel agents than from the airlines.

According to "The 1998 ASTA Consumer Travel Purchase Report," a study conducted for ASTA by Plog Research, Inc., air travelers place greater trust in travel agents than any other travel information source, and technology makes no comparable improvement in credibility for the most experienced travelers. Given the credibility achieved by travel agents, the Plog study concluded, it follows that travelers believe that the best way to insure that they get the travel products and services they desire is to use a travel agent when making air travel purchases.

Because they are already the public's overwhelming choice as a source for travel information and arrangement expertise, there is every reason to believe that travel agents can also deliver air transportation services more efficiently over the Internet and through other electronic systems than can major airlines. Nonetheless, major airlines appear determined to reduce or eliminate the role of travel agents and other independent distributors' in the information, sales and distribution process regardless of the medium.

Elimination or reduction of independent distributors by airlines will eliminate the public's access to efficient comparative schedule and fare information, its access to efficient reservations services, and access to efficient ticketing services (paper or electronic). If the major airlines are successful, consumers will be confronted with a very limited selection of inefficient, highly biased, airline-owned and operated information and distribution systems.

### **Airlines as a Law Unto Themselves – Federal Preemption of State Law**

When Congress deregulated the airline industry by passage of the Airline Deregulation Act of 1978, it prohibited states from "enact[ing] or enforc[ing] any law \*\*\* relating to rates, routes, or services." 49 U.S.C. App. 1305(a)(1). Obviously, such a provision was necessary to prevent the states from subjecting to their regulation that which

Congress had just removed from federal regulation. That federal preemption provision, shielding airlines from state regulation, has now been turned by the airlines into a sword with which they bar the general public and small businesses from holding them accountable under the same state law that applies to every other industry in the country. The result is that the airlines have become a veritable law unto themselves, immune from state-law suits seeking to hold them responsible for harm to passengers as well as their obligations to small businesses. At the same time, the airlines remain free to call upon, and do call upon, these same state law principles against other parties when their own interests are served.

Although observing that the treatment to which a passenger had been subjected was “ unquestionably rude and unprofessional,” the U.S. Court of Appeals for the Fourth Circuit, in the recent case of Smith v. Comair, Inc. and Delta Airlines, Inc., No. 96-2451, decided January 15, 1998, \_\_\_ F.3d \_\_\_, held that Federal preemption barred the passenger from suing the airlines for refusing him permission to board his flight.

Similarly, a suit by a travel agent against an airline for harming its business was halted by the U.S. District Court at Dallas on Federal preemption grounds in Lyn-Lea Travel Corp. v. American Airlines, Inc., No. CA3:96-CV-2068-BC, decided December 2, 1997. The court ruled that state law claims for tortious interference, deceptive trade practices, fraud and breach of contract could not go forward, leaving the travel agent with no forum for its claims except the Department of Transportation (“DoT”). The Government itself, however, has previously conceded that DoT has neither the authority nor the apparatus required to superintend a dispute resolution regime, especially one involving claims for damages. American Airlines, Inc. v. Wolens, 513 U.S. 219 (1995) at 232.

The difficulties and lack of consensus experienced by judges struggling to define the scope of the Airline Deregulation Act’s preemption provision is further illustrated by the case of Hodges v. Delta Airlines, Inc., twice before the U.S. Court of Appeals for the Fifth Circuit.

Frances Hodges was injured on a flight from the Caribbean to Miami, when a fellow passenger opened the overhead compartment directly above her seat, dislodging and spilling a case containing several bottles of rum. The box fell on Ms. Hodges, lacerating her left arm and wrist. Before her profuse bleeding was brought under control, a significant amount of her blood mingled in the aisle with the puddle of rum and broken glass.

Bound by previous precedent, a Fifth Circuit panel held that Federal preemption barred Ms. Hodges’ suit against the airline. It quickly added, however, that it believed this result to be wrong, and urged that all of the Circuit’s judges re-hear the case, en banc. Hodges v. Delta Airlines, Inc., 24 Avi. 17,722 (1993).

On rehearing, the Fifth Circuit overruled its prior decision in Baugh v. Trans World

Airlines, Inc., 915 F.2d 693 (5th Cir.1990), on the basis of which the panel had felt bound to dismiss the passenger's suit. Even here, however, separate opinions reflect at least three different views of the scope of preemption held among Fifth Circuit judges. Hodges v. Delta Airlines, Inc., 24 Avi. 18,361 (1995).

Noting that the statements of the Civil Aeronautics Board implementing airline deregulation, strongly support the view that the Airline Deregulation Act was concerned solely with economic deregulation, not with displacing state tort law, the en banc Fifth Circuit held that Federal preemption did not displace state tort actions for personal, physical injuries or property damage caused by the operation and maintenance of aircraft.

Two judges disagreed, holding that the scope of Federal preemption was broader and barred Ms. Hodges' suit.

Concurring in the result, Judge E. Grady Jolly, observed that the very fact the majority and the dissent disagreed only on the application of the principle that a claim is preempted if it relates to services that are not a part of the maintenance or operation of an airline, reveals that such a rule promises uncertain and inconsistent results.

In Judge Jolly's view, suits involving efforts by private individuals to obtain relief afforded by state common law tort rules are not instances of a state imposing its own substantive standards with respect to rates, routes, or services, which is what the Airline Deregulation Act was meant to preempt.

The broad interpretation some judges have given Federal preemption under the Act also has not escaped criticism from Justices of the Supreme Court, including the Chief Justice of the United States.

Speaking as well for the Chief Justice and Justice Blackmun, Justice Stevens has written:

the presumption against preemption of traditional state regulation counsels that we not interpret 105(a) to pre-empt every traditional state regulation that might have some indirect connection with, or relationship to, airline rates, routes, or services unless there is some indication that Congress intended that result. To determine whether Congress had such an intent, I believe that a consideration of the history and structure of the ADA is more illuminating than a narrow focus on the words "relating to." Morales v. Trans World Airlines, Inc., 504 U.S. 374 (1992) at 421 (Stevens, J., dissenting).

Differences of interpretation in the scope of the Federal preemption that several Justices of the Supreme Court would accord airlines under the Airline Deregulation Act, as well as instances of members of the public and small businesses being denied a forum for their claims, illustrate clearly that clarification and modification of this

troublesome provision must be undertaken.

ASTA supports statutory language it believes strikes the appropriate balance between the airlines' need to be free of state economic regulation of fares and routes in a deregulated environment, and the rights of consumers and others to have redress against airlines for their failures to abide by the same state law standards of conduct all other parties must observe.

That language amends 49 U.S.C. Section 41713(b) by providing:

**This subsection shall not bar any cause of action brought against an air carrier by one or more private parties seeking to enforce any right under the common law of any State or under any State statute, other than a statute purporting to directly prescribe fares, routes, or levels of air transportation service.**

This language currently appears as Section 7 of S. 477, the "Airline Competition Act of 1999," offered by Senator Schumer, and as Section 9 of H.R. 272, the "Airline Competition and Lower Fares Act," offered by Representative Slaughter, and is appropriate for inclusion in other consumer aviation legislation.

## Conclusion

Independent providers of travel services are absolutely necessary for optimal consumer welfare. Consumers derive substantial benefits from the presence of travel agents in the travel service market. Among other functions, agencies provide accurate, unbiased and convenient sources of information and services involving airline and other travel suppliers' schedules, rates and ticketing. Because no single airline is able or willing to offer free and ready access to comparative information, the only source of information for consumers who want to choose a carrier by assessing the best value in terms of place/time/price is an independent agency. Overall, for these and many other reasons, the traveling public has historically judged travel agencies as a far more efficient and reliable source of travel services than carriers.

Both economic theory and recent history teach a clear and important lesson: the firms that comprise the U.S. airline oligopoly are prone to anti-competitive acts of predation and collusion.<sup>7</sup> Their past conduct demands constant and heightened scrutiny of their practices toward travel agencies.

The acts and practices we have discussed threaten permanent injury to the competitive process and, unchecked, will result in the transfer to the major carriers of vast amounts of wealth that consumers would otherwise enjoy. These and other carrier-imposed restraints deny to travel agencies the freedom to take independent actions that would make their operations more efficient and responsive to consumer demand.

By restricting travel agency output, these restraints also enable individual carriers to exercise power over price in discrete geographic markets for air transportation. Taken together, their aggregate effect is to allow carriers collectively to overcharge consumers on the order of hundreds of millions of dollars more annually than they could earn under fully competitive conditions – a rate of welfare loss that will only increase over time unless the carriers' anti-competitive conduct is stopped.

By restraining the competitiveness of an industry segment that serves all travel suppliers, not just airlines, the long-run welfare loss is even more severe than the loss extracted by a single monopolist that overcharges customers by setting price above its marginal costs.

At its core, and as a whole, the carriers' anti-competitive strategy is designed to erode the ability and incentives of consumers to seek and obtain the services of travel

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<sup>7</sup>See for example, U.S. v. Airline Tariff Publishing Co., 1993-1 Trade Cas. (CCH) ¶170,191 (D.D.C., 1993).

agencies, including emergent on-line booking services and auction sites. The airlines know and have acted upon the fundamental truth that when consumers are deprived of comparative information in making travel purchases, they almost always end up paying more not because fares rise in absolute terms but rather because consumers are unaware of lower fares and are therefore not able to claim them. Simply put, carrier practices that even modestly reduce competition from travel agencies produce immediate and out-sized gains in carrier profitability, not because of increased efficiency but by exploitation of consumers' inability to obtain the lowest price when dealing directly with them.

The importance and urgency of the Committee's work is highlighted by the charts we have set forth as Attachment A. They mark the success of the implementation of the airlines' strategy for reducing competition by undermining travel agents' ability to effectively fulfil their traditional role of moderating the adverse effects on consumers resulting from the high degree of concentration in the airline industry. Also attached, as Attachment B, is a front page article from a year-end edition of the Washington Post, which reflects the high degree of concern this situation is engendering among the general public.

ASTA appreciates the opportunity to have presented its views, and remains at the Committee's disposal to assist in any way it can.

Respectfully submitted.

Operating Officer -- Acting

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## **Attachment B**

### **Travel Agents Feel the Squeeze Internet, Low Commissions Putting Firms Out of Business**

By Judith Evans  
Washington Post Staff Writer  
Sunday, December 27, 1998; Page A01

It's a typical day for travel agent Denise Foster. She moves her hands nimbly across her keyboard as she begins arranging a three-day business trip for a client. She types in arcane codes that prompt airline flight schedules to appear on her computer monitor.

She finds her client a flight from Phoenix to Chicago so that he can arrive in time to deliver a speech and shake hands with a few people in the audience before heading out to New York. He'll give a morning speech in Manhattan, then fly back to Chicago to meet clients the next morning. That evening, he'll fly back home to Phoenix.

Foster spends more than 30 minutes coordinating flights to ensure they accommodate her client's tightly packed schedule. The client will pay \$3,764 for the trip. For her work, Foster will earn a \$50 commission paid by the airlines. Three years ago, before airlines began cutting commissions, her company would have made \$376.40.

"You see how hard my girls work for so little money," says Michael MacNair, who owns MacNair Travel Management/American Express, where Foster works. The agency, with offices in the District and Alexandria, generates \$20 million a year in revenue.

So far, MacNair Travel is surviving the competitive pressures facing an industry that many experts believe will eventually get squeezed out of existence. Travel agencies nationwide are facing ferocious competition from online travel services, while at the same time their once-friendly relationships with hotel and car rental companies are deteriorating. To top it off, airlines have cut the commissions they pay to travel agents three times in two years and are poised to do so again on international routes.

Since World War II, travel agencies have positioned themselves as the most efficient peddlers of travel information. But that paradigm is crumbling. Unable to make enough money in a business already pressured by low profit margins and high labor costs, fewer people are opening agencies. Five firms in the Washington area recently filed for bankruptcy.

Some agencies have sold their operations to larger companies so they can reduce their operating expenses and get better prices from suppliers. A growing number have begun charging consumers for services that once were considered free for the price of their tickets. Other agencies are offering new services, such as travel management and events planning.

"A lot of what is spurring this is how travel suppliers like airlines, car companies and hotels want to secure the fidelity of their customers," says Nick Athanasio, vice president and director of Arthur D. Little's travel industry practice. "Over the short term, many of them are more than willing to pay higher internal costs to transact with the customer."

Airlines, car companies and hotels have discovered the Internet is an inexpensive way to reach out to consumers and to track their travel preferences. More than three-quarters of the top 75 airlines, hotels and car rental companies offer online booking on their World Wide Web sites, according to a recent report by Forrester Research Inc.

With the click of a mouse, consumers can find bargain air fares to Las Vegas and detailed reports on Bali, 24 hours a day, seven days a week. Consumers will book an estimated 8.2 million leisure trips online in 1998, generating \$3.1 billion in revenue. The report estimates sales will grow to \$29 billion by 2003.

Travel booking is the largest online consumer retail segment in dollar volume, eclipsing the sale of books, music and computers. "Travel, more than any other product, is an information-heavy service," says James McQuivey, an analyst in online retail strategies for Forrester. "Information is the Internet's specialty. Travel can be the most convenient Internet shopping. You can do it any time and get immediate confirmation."

Some travel agencies, particularly discount consolidators, say the online services put them at a competitive disadvantage. For instance, many airlines run special promotions to consumers, with discounted air fares and hotel stays that aren't as readily available to the general public. The air fares for international trips can often be 20 percent to 30 percent lower than those offered by discount agencies, consolidators said.

It's difficult to quantify how much business the Internet is taking away from travel agencies, but Jane Sutter isn't waiting to find out. As president of Empress Premier Travel, Sutter is changing her agency into one that specializes in leisure travel, where commissions for cruises and vacation packages have not been slashed. She also relocated her agency, which generates \$3 million a year in revenue, to Vienna, in part to appeal to that

community's more affluent travelers. Sutter believes higher-income travelers are less likely to use the Internet because they want personal recommendations about hotels and exotic travel spots. She's making sure that her agents can provide that service by sending them on trips to the Caribbean and other popular destinations.

"I think people, even with Internet, want a little personal touch when spending such a significant amount of money," Sutter says. "The only thing that we have differently from the Internet is service."

Still, Sutter has her doubts about competing with the online behemoth. "Sometimes it's frustrating and you have to decide whether the business is worth pursuing or whether it will beat you," she says.

With consumers increasingly embracing online travel, airlines perceived an opportunity to reduce the commissions they paid to agents, tourism experts say. Travel agents sell nearly 85 percent of all airline tickets. Agents' commissions rank as the airline industry's third-largest operating expense, after fuel and labor costs.

The airlines believe they can chip away at the agencies' dominance in selling tickets now that consumers have more alternatives to purchase them, tourism experts say. A year ago, several major airlines cut commissions on domestic tickets to 8 percent from 10 percent and then capped the maximum commission at \$50 for a round-trip ticket.

Recently, United Airlines, American Airlines and Delta Air Lines cut commissions on international flights to 8 percent from 10 percent and added caps of \$100 per round trip. Amtrak, too, has reduced its commissions to agents to 8 percent.

The cuts have been particularly harsh on agencies like MacNair, where about 70 percent of the revenue comes from corporate clients. Michael MacNair estimates that he will lose nearly \$75,000 a year in commissions as a result of United's latest rate reduction.

He says the international cut is difficult to get around because his government-contractor clients will not fly on foreign carriers. The commission cuts also have led him to revise his company's business plan again. "I feel like I've been an entrepreneur three different times with the same business," MacNair says.

MacNair this past year paid a hefty fee to affiliate his agency with American Express. That has helped boost the agency's leisure business to around 30 percent of its total. He's expanded services to provide

customers with travel management and meeting planning. He's also offering his agents incentives to work more productively, paying them a combination of base salaries and performance bonuses.

"I must sell more in the future in order to survive," MacNair says.

Many travel agencies are starting to charge fees, which can be a tricky proposition as more information is made available to on the Internet for free. In a recent survey by the American Society of Travel Agents, 64 percent of those agencies that responded charge consumers an average fee of \$10.37 to book airline tickets. Consumers also can expect to pay other fees for bookings that include use of a special coupon or promotions, refunds and exchanges.

Nearly 85 percent of the agents charging fees began doing so after the latest round of cuts, saying commissions don't cover the costs associated with making airline reservations. Before the first commission cuts in 1995, only 2.6 percent of agencies said they charged fees.

Michael MacNair created three different fee schedules for his customers, depending on the amount of business they do annually with the agency. While large corporate clients don't pay a fee, smaller businesses are charged one for each transaction. "We lost one client," he says, when the company moved to fees two year ago. "Since then we've lost a couple more. But that's okay. I'm here to run a business, not a charity."

To justify the fees, American Express agencies are seeking to provide customers with better service and more information. Employees at reservation centers have been divided into teams, which are responsible for a specific number of customers. Whenever the customer calls the toll-free number, they should get an agent who is familiar with their travel history.

"The fundamental shift I see is that travel agents are aligning much more tightly with the consumer," says Marianne Toldalagi, senior vice president and general manager for leisure travel at American Express Travel Related Services Inc. "In the past, we were agents for the suppliers."

American Express has unveiled a new feature on its Web site, listing the names and phone numbers of customer service representatives knowledgeable about certain destinations. "Customers want to reach us any way they can, whether electronically, by phone or visiting one of our offices," Toldalagi says. "That's the marketplace. We want to play all the distribution channels."

American Express has made similar changes in its corporate travel

business, which generates the majority of the group's revenue. In some cases, the business travel division has terminated agreements where it shared commissions with its corporate clients.

The company also now allows customers to pay a fee based only on the services they actually use, which can save them money.

Corporate clients can also cut their expenses by installing desktop software that allows employees to book their own travel. The software contains security features so employees don't book first-class travel when it's against their company's policy. About 125,000 corporate clients are using the system.

But some agencies aren't sure how long they can survive even if they change their business practices. Sutter has not been able to take a salary from her business for two years. Her partner left last year. She says the changes she has made to her business have cost her \$20,000 in salary and training for her staff.

"There are times when I, financially, don't see the rewards," Sutter says.

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